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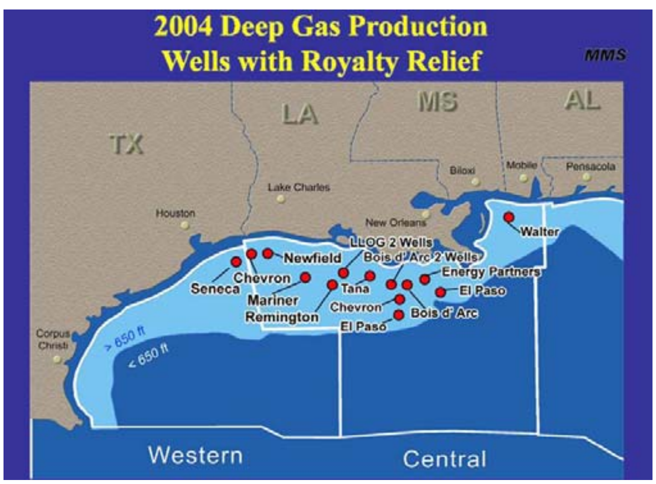
Energy Production Incentives: A Step Toward Greater Energy Independence for America

In an effort to decrease U.S. dependence on foreign sources of energy, Congress enacted the Deep Water Royalty Relief Act (DWRRA) in 1995. In essence, the act is a call for energy companies to increase their exploration efforts to reach areas of the Federal waters of the Outer Continental Shelf (OCS) in order to meet America's growing demand for oil and gas.

The Act also allows additional royalty relief – called Royalty Suspension Volumes (RSVs) – for leases located in water depths of more than 200 meters in the Central and Western Gulf of Mexico, if the lessee can demonstrate an economic need for royalty relief.



After 2000, the MMS revised many of the technical aspects of deep water royalty relief so that relief could be granted by water depth on a sale-by-sale basis, which led to still more energy exploration, even in areas that had been previously considered marginal.

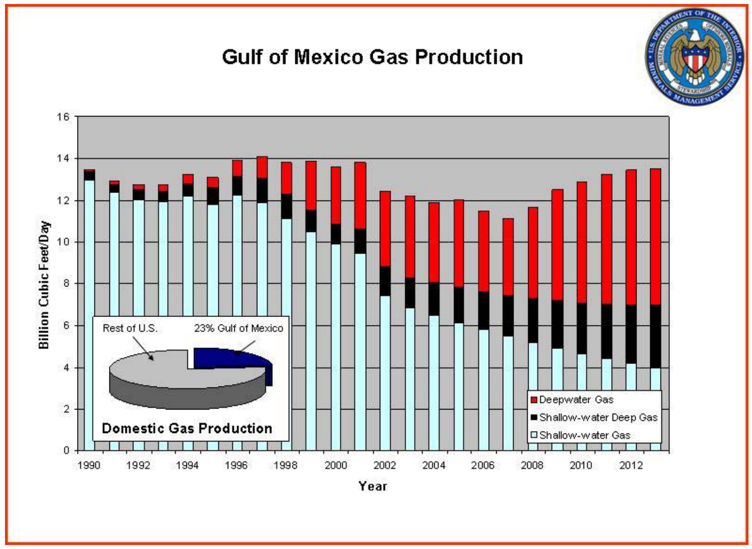
The benefit of this incentive is in the numbers. Since the DWRRA was passed, oil production in water deeper than 200 meters has increased by about 550 percent through 2004 – now standing at over 350 million barrels a year – representing more than 60 percent of total Gulf of Mexico oil production. About one-third of the deep water production in 2005 is expected to occur from leases sold under the DWRRA.

The news is just as good for natural gas, where production in deep waters has increased by about 650 percent between 1995 and 2004, and currently stands at more than 1.4 trillion cubic feet per year.

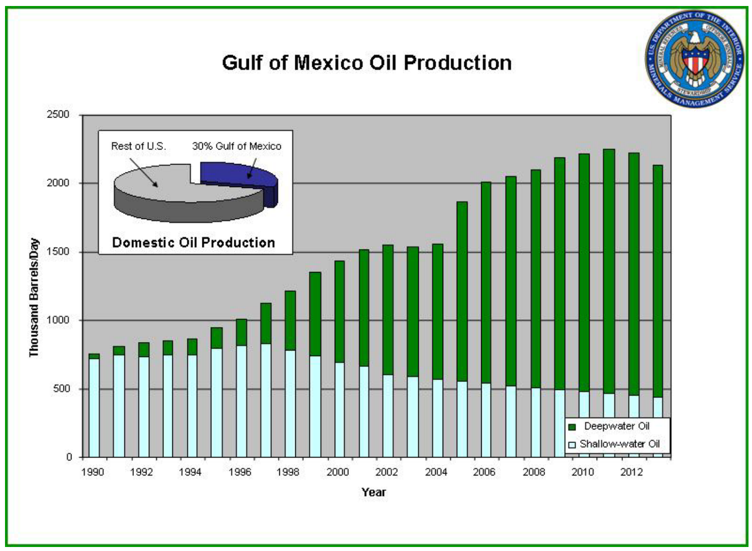
Additional incentives to go deeper in search of natural gas have brought additional positive results. Incentives announced in 2001 and modified in 2004 encourage energy companies to use equipment that is already in place in shallow waters to explore deeper, at least to 15,000 feet. "Deep depth gas production" is expected to increase and become a much larger portion of all gas produced in the Gulf of Mexico.

Deep depth gas production is expected to become a larger proportion of all gas produced over the next 10 years in the Gulf of Mexico. For 2005, it is predicted that 10 percent of all natural gas production in the Gulf will come from deep depth wells on leases issued with deep gas relief or on leases affected by the deep gas regulations. This percentage is anticipated to double to 20 percent over the next decade.

The emerging presence of substantial quantities of deep depth gas, in conjunction with relatively closed domestic gas market conditions, results in a heating bill benefit to consumers. The MMS estimates that access to this additional supply will lower domestic natural gas prices by almost one cent per million cubic feet. The MMS energy experts have also determined that the fiscal effect from such a price decline could mean a savings to consumers of more than $500 million per year over the next ten years.



Furthermore, MMS believes that the royalty relief programs implemented under the DWRRA encourage additional exploration and development of economically marginal offshore resources, thereby increasing domestic reserves of oil and natural gas. And even if all production on leases issued under the DWRRA is generated royalty free, notwithstanding the other MMS designed royalty relief programs, the majority of total offshore oil and gas production will continue to pay royalties over the next decade.



What does this mean for America? It means savings for consumers. It means a lower monthly energy bill. It means energy from a domestic, stable source.